

**Fiscal Year 2003 Statutory Audit of  
Compliance With Notifying Taxpayers of  
Their Rights When Requested to Extend the  
Assessment Statute**

**September 2003**

**Reference Number: 2003-40-193**

**This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.**



DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

INSPECTOR GENERAL  
for TAX  
ADMINISTRATION

September 11, 2003

MEMORANDUM FOR COMMISSIONER EVERSON

*Gordon C. Milbourn III*

FROM: Gordon C. Milbourn III  
Assistant Inspector General for Audit (Small Business and  
Corporate Programs)

SUBJECT: Final Audit Report - Fiscal Year 2003 Statutory Audit of  
Compliance With Notifying Taxpayers of Their Rights When  
Requested to Extend the Assessment Statute  
(Audit # 200240065)

This report presents the results of our review to determine if the Internal Revenue Service (IRS) is in compliance with Internal Revenue Code (I.R.C.) Section (§) 6501(c)(4)(B) (Supp. IV 1998),<sup>1</sup> which requires the IRS to provide notice to taxpayers of their right to decline to extend the assessment statute of limitations or to request that any extension be limited to a specific period of time or to specific issues.

The Treasury Inspector General for Tax Administration is required to provide information annually regarding the IRS' compliance with I.R.C. § 6501(c)(4)(B). The IRS is required to advise taxpayers of their rights when requesting an extension of the statute of limitations on assessment of additional tax and penalties. In passing this law, the Congress expressed concern that taxpayers were not being adequately advised of their right to refuse to extend the statute of limitations or to request that a statute extension be limited to a specific period of time or to specific issues.

In summary, employees properly advised taxpayers of their right to refuse or to restrict the scope of the statute extension in 113 (74 percent) of the 153 tax returns sampled. However, for the remaining 40 (26 percent) tax returns, we could not determine if employees advised taxpayers of their rights because related case files did not contain a record that taxpayers had been so advised. In addition, in 37 (63 percent) of the 59 jointly filed returns in our sample of 153 returns, there was no documentation in the related case files that each taxpayer listed on the return was separately informed of his

---

<sup>1</sup> I.R.C. § 7803(d)(1)(C) (Supp. IV 1998).

or her rights (i.e., dual notification). Finally, in 57 (52 percent) of the 109 tax returns in which taxpayers had made a declaration of representation in our sample of 153 returns, there was no documentation in the related case files that the IRS had provided both the taxpayer and the representatives with the advice of rights. Some of the 153 sampled tax returns and related case files met multiple criteria.<sup>2</sup> At this time, the procedures and proposed internal guidelines the IRS has provided its employees should ensure that they adequately document that taxpayers are advised of their right to refuse or to restrict the scope of the statute extension. Therefore, we are making no recommendations at this time.

Management's Response: IRS management agreed with our conclusion that, in most situations, the IRS is appropriately advising taxpayers and representatives of their rights. They acknowledged that some case files lacked specific written documentation, but indicated that during a follow-up review they found other documentation in the case file that showed the taxpayers had received satisfactory notification of their rights. Management's complete response to the draft report is included as Appendix VII.

Office of Audit Comment: In the response, IRS management stated that as part of a follow-up review, they found other documentation in the case files that showed that the taxpayers had received satisfactory notification of their rights. After further discussion with IRS management, they advised us that a follow-up review had not been performed.

Copies of this report are also being sent to the IRS managers who are affected by the report results. Please contact me at (202) 622-6510 if you have questions, or your staff may call Michael R. Phillips, Assistant Inspector General for Audit (Wage and Investment Income Programs), at (202) 927-0597.

---

<sup>2</sup> All cases do not have the same requirements. For example, all cases have a documentation requirement; however, not all cases involve taxpayer representatives or those who file joint returns.

**Fiscal Year 2003 Statutory Audit of Compliance With Notifying Taxpayers  
of Their Rights When Requested to Extend the Assessment Statute**

---

**Table of Contents**

Background .....	Page 1
Most Related Case Files Documented That Taxpayers or Their Representatives Were Advised of Their Rights Regarding Assessment Statute Extensions .....	Page 3
Compliance With Dual Notification Requirements Needs Improvement.....	Page 6
Compliance With Procedural Regulations Needs Improvement .....	Page 7
Appendix I – Detailed Objective, Scope, and Methodology .....	Page 9
Appendix II – Major Contributors to This Report.....	Page 11
Appendix III – Report Distribution List .....	Page 12
Appendix IV – Outcome Measures .....	Page 13
Appendix V – Case Review Results by Division .....	Page 14
Appendix VI - Listing of Prior Reports on Compliance With Notifying Taxpayers of Their Rights When Requested to Extend the Assessment Statute.....	Page 15
Appendix VII - Management’s Response to the Draft Report .....	Page 16

## **Fiscal Year 2003 Statutory Audit of Compliance With Notifying Taxpayers of Their Rights When Requested to Extend the Assessment Statute**

---

---

### **Background**

---

The Internal Revenue Service (IRS) is required by Internal Revenue Code (I.R.C.) Section (§) 6501(c)(4)(B) (Supp. IV 1998)<sup>1</sup> to advise taxpayers of their rights whenever requesting an extension of the statute of limitations on assessment of additional tax and penalties. In passing this law, the Congress expressed concern that taxpayers were not being adequately advised of their right to refuse to extend the statute of limitations or to request that a statute extension be limited to a specific period of time or to specific issues.

In addition, the IRS Restructuring and Reform Act of 1998 (RRA 98)<sup>2</sup> § 3201 requires the IRS to send any notice relating to a jointly filed return separately to each individual filing the joint return. Federal regulations require that any notice or other written communication (or copy) required or permitted to be given to a taxpayer in any matter before the IRS must also be given to the taxpayer and, unless restricted by the taxpayer, to the taxpayer's representative.<sup>3</sup>

If the IRS examines a tax return and determines there is an additional tax liability, it generally must be assessed within 3 years from the date that a return was due or the date that the return was actually filed, whichever is later. This 3-year assessment statute of limitations normally cannot be extended without the taxpayer's written agreement.<sup>4</sup>

To extend the assessment statute, the IRS asks the taxpayer to sign a statute extension agreement form (consent).<sup>5</sup> A consent extends the assessment statute of limitations to either a specific date or for an unlimited, indefinite period. The statute is usually extended for a period that both the IRS and the taxpayer agree is reasonable to complete the

---

<sup>1</sup> I.R.C. § 7803(d)(1)(C) (Supp. IV 1998).

<sup>2</sup> Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

<sup>3</sup> 26 Code of Federal Regulations § 601.506 (2001).

<sup>4</sup> There are some exceptions to the 3-year statute of limitations. For example, I.R.C. § 6501(c)(1) (1994) extends the assessment statute indefinitely when false or fraudulent returns are filed.

<sup>5</sup> IRS employees who most often request assessment statute extensions are examiners in the Examination function of the operating divisions and appeals officers in the Office of Appeals.

## **Fiscal Year 2003 Statutory Audit of Compliance With Notifying Taxpayers of Their Rights When Requested to Extend the Assessment Statute**

---

examination. The consent can also be negotiated to apply only to certain examination issues.

A taxpayer might agree to extend the assessment statute of limitations for the following reasons:

- The taxpayer may want to pursue additional examination issues that are in the taxpayer's favor in offsetting a proposed tax or that might allow for a tax refund.
- If the remaining time before the statute expires is too short, the IRS may have to prematurely stop the examination process and issue a notice of deficiency that limits the time for the normal appeals process before the taxpayer must file a petition to the United States Tax Court.

There are also certain circumstances when a taxpayer may decide to limit or refuse to extend the assessment statute of limitations:

- The taxpayer may not want to provide the IRS additional time to consider additional examination issues.
- The taxpayer may not want to allow the IRS the opportunity to further develop examination issues already under consideration after the normal statute period has expired.

The Treasury Inspector General for Tax Administration is required to provide information annually regarding the IRS' compliance with I.R.C. § 6501(c)(4)(B). This report presents the results of our fourth annual review of the IRS' compliance with the statute extension provisions of the law. In the prior reviews, we evaluated assessment statute extensions processed from January 1 to March 24, 2000; April 1 to September 30, 2000; and October 1, 2000, to September 30, 2001, respectively. See Appendix VI for a list of prior issued reports.

We reported that in the majority of the related case files reviewed, IRS employees advised taxpayers of their rights to refuse or restrict the scope of the statute extension. However, we also reported that improved documentation was needed to ensure taxpayers were informed of their rights. In response, the IRS agreed to update guidelines,

## Fiscal Year 2003 Statutory Audit of Compliance With Notifying Taxpayers of Their Rights When Requested to Extend the Assessment Statute

---

revise *Extending the Tax Assessment Period* (Publication 1035) used to notify taxpayers of their rights, and inform employees of the changes.

For the current audit, we reviewed assessment statute extensions processed from September 30, 2001, to October 5, 2002. This review was performed in the Large and Mid-Size Business Division Headquarters, the Office of Appeals Headquarters, and the Tax Exempt and Government Entities Division Headquarters in Washington, D.C., and the Small Business/Self-Employed (SB/SE) Division in New Carrollton, Maryland.

We performed the audit between February and June 2003 in accordance with *Government Auditing Standards*. Detailed information on the audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

---

### Most Related Case Files Documented That Taxpayers or Their Representatives Were Advised of Their Rights Regarding Assessment Statute Extensions

---

For 113 (74 percent) of the 153<sup>6</sup> tax returns in our judgmental sample, IRS employees advised taxpayers or their representatives of their right to refuse or to restrict the scope of the statute extension. The consents<sup>7</sup> do not currently provide an explanation of the taxpayers' right to limit or refuse to extend the assessment statute of limitations. Therefore, we considered that IRS employees advised taxpayers of their rights if any of the following documentation was found in the related case files:

- A copy of *Request to Extend Statute of Limitation Period* (Letter 907 (L-907)), *Letter Transmitting Consent Extending Period of Limitation* (Letter 967 (L-967)), or comparable cover letter updated to include an explanation of taxpayer rights.
- A record that Publication 1035 was provided to the taxpayer and/or representative, as documented in the examination activity record or as shown as an enclosure

---

<sup>6</sup> See Appendix V for a breakdown of the requests by division.

<sup>7</sup> The IRS uses several different types of consents, depending on the type of tax involved. For example, *Consent to Extend the Time to Assess Tax* (Form 872) is used for income taxes, and *Consent to Extend the Time to Assess Employment Taxes* (Form SS-10) is used for employment taxes.

## **Fiscal Year 2003 Statutory Audit of Compliance With Notifying Taxpayers of Their Rights When Requested to Extend the Assessment Statute**

---

on a cover letter. This publication provides a detailed explanation of taxpayer rights.

- The examination activity record showed the taxpayer and/or representative was given the required notification of rights.

For the remaining 40 (26 percent) of 153 tax returns sampled, the related case files did not contain documentation that taxpayers had been advised of their rights. As a result, we could not determine if the IRS protected the right of these taxpayers to be advised of their statute extension options. This occurred because employees were not following IRS internal guidelines.

For 17 of the 40 tax returns, the IRS requested multiple extensions. Although the IRS advised taxpayers of their rights for extension requests at some time during the examination, there was no record in the related case files documenting that the taxpayers were notified of their rights for the last extensions requested. Even though the IRS did not comply with I.R.C. § 6501 for each and every extension in these cases, we believe the legislative purpose of the section was fulfilled, i.e., the taxpayers had an understanding of their rights.

I.R.C. § 6501 provides that the IRS must notify the taxpayer of his or her rights on each occasion when the taxpayer is requested to consent to an extension. It would be a potential violation of taxpayers' rights if the IRS did not notify taxpayers of their options when requesting assessment statute extensions. If taxpayers are not notified of their rights, they might not be aware that they have the right to refuse to extend the period of limitations or to limit such extensions to particular items or particular periods of time.

### **Employees were not always following IRS internal guidelines on the documentation needed to ensure taxpayers were advised of their rights**

Although 113 of the 153 related case files contained enough documentation to determine that IRS employees advised taxpayers or their representatives of their right to refuse or to restrict the scope of the statute extension, 114 (75 percent) of the 153 related case files did not contain



## **Fiscal Year 2003 Statutory Audit of Compliance With Notifying Taxpayers of Their Rights When Requested to Extend the Assessment Statute**

---

all the documentation required by the IRS. The Examination function manual covering the examination of tax returns requires that when IRS employees request a taxpayer to extend the assessment statute, they provide the taxpayer with an L-907 (maintaining a copy of the letter in the related case files) and a Publication 1035 as an enclosure. They also must document on an activity record whether the taxpayer was notified of his or her rights. In response to our September 2000 report, the IRS issued guidance stating that, effective February 28, 2002, the L-907, L-967, and executed consent must be attached to each return covered by the extension. The IRS is also in the process of revising its internal procedures manual to include these new guidelines.

The Appeals function manual requires that the L-967 be used to advise the taxpayer that the statute is about to expire and transmit the consent forms for execution. The L-967 and executed consent are to be attached to each return covered by the extension. While the Appeals manual does not address the documentation required on the case activity record, Appeals/Settlement Officers were reminded in a May 9, 2002, memorandum that they should continue to annotate the case activity record that the taxpayer was provided with an explanation of rights regarding the extension.

At this time, we believe the procedures and proposed internal guidelines the IRS has provided its employees should ensure that they adequately document that taxpayers are advised of their right to refuse or to restrict the scope of the statute extension. Therefore, we do not believe the risk warrants additional procedures or reviews and are making no recommendations at this time. However, if the errors in documentation do not decline, the IRS might consider revising the consents to include an explanation of the taxpayers' rights regarding statute extensions.

## **Fiscal Year 2003 Statutory Audit of Compliance With Notifying Taxpayers of Their Rights When Requested to Extend the Assessment Statute**

---

---

### **Compliance With Dual Notification Requirements Needs Improvement**

---

For 37 (63 percent) of the 59 jointly filed returns sampled, there was no documentation in the related case files that each taxpayer listed on the return was separately informed of his or her rights (i.e., dual notification).<sup>8</sup> This occurred because employees were not following IRS internal guidelines.

RRA 98 § 3201 requires the IRS to send any notice relating to a jointly filed return separately to each individual filing the joint return. The Congress intended that separate notices would increase the likelihood that separated or divorced spouses receive such notices, as well as increase the likelihood that the IRS will be made aware of address changes that apply to one, but not both, spouses. There could be a violation of taxpayer rights if both taxpayers were not notified of their right to refuse to extend the period of limitations or to limit such extensions to particular items or particular periods of time.

The Examination manual states that any notice relating to a jointly filed return should be separately mailed to each individual filing the joint return. In addition, Examination function management included an article in the January 2003 issuance of the IRS Technical Digest advising employees of the importance of dual notification.

The Appeals manual does not address dual notification. However, IRS officials issued memoranda on October 28, 1998, and May 13, 1999, that required dual notification for all jointly filed returns. Appeals function management informed us during a prior audit that they would revise their manual to include dual notification requirements, but at the time of this review this revision had not been made.

While the Office of Appeals has not yet revised its manual, the IRS is finalizing revisions to the manual providing guidelines to all divisions; these revisions include a requirement to provide notice to both taxpayers on jointly filed returns. We do not believe the risk concerning dual

---

<sup>8</sup> Some of the 153 sampled tax returns and related case files met multiple criteria.

## **Fiscal Year 2003 Statutory Audit of Compliance With Notifying Taxpayers of Their Rights When Requested to Extend the Assessment Statute**

---

---

### **Compliance With Procedural Regulations Needs Improvement**

---

notification warrants additional procedures or reviews and are making no recommendations at this time.

For 57 (52 percent) of the 109 tax returns sampled where taxpayers made a declaration of representation, there was no documentation in the related case files that the IRS had provided both the taxpayers and their representatives with the advice of rights.<sup>9</sup> Again, this occurred because employees were not following IRS internal guidelines.

Current IRS manual guidelines and Federal regulations require that any notice or other written communication (or copy) required or permitted to be given to a taxpayer in any matter before the IRS must also be given, unless restricted by the taxpayer, to the taxpayer's representative.

Taxpayer rights or taxpayer burden could be affected if the IRS does not follow the Federal regulations and provide both the taxpayer and the taxpayer's representative with the right to refuse to extend the period of limitations or to limit such extensions to particular items or particular periods of time.

However, we believe the current guidelines are appropriate and adequate. Considering the minimal risk, we are making no recommendations concerning representative notification at this time.

Management's Response: Management agreed with our conclusion that, in most situations, the IRS is appropriately advising taxpayers and representatives of their rights. They acknowledged that some of the case files lacked specific written documentation, but indicated that during a follow-up review they found other documentation in the case file that showed the taxpayers had received satisfactory notification of their rights.

Office of Audit Comment: In their response, IRS management stated that as part of a follow-up review, they found other documentation in the case files that showed that

---

<sup>9</sup> Some of the 153 sampled tax returns and related case files met multiple criteria.

**Fiscal Year 2003 Statutory Audit of Compliance With Notifying Taxpayers  
of Their Rights When Requested to Extend the Assessment Statute**

---

the taxpayers had received satisfactory notification of their rights. After further discussion with IRS management, they advised us that a follow-up review had not been performed.

### **Detailed Objective, Scope, and Methodology**

The overall objective of this review was to determine whether the Internal Revenue Service (IRS) was complying with Internal Revenue Code (I.R.C.) Section (§) 6501(c)(4)(B) (Supp. IV 1998), which requires the IRS to provide notice to taxpayers of their right to decline to extend the assessment statute of limitations or to request that any extension be limited to a specific period of time or to specific issues. To accomplish our objective, we:

- I. Determined whether taxpayers were being advised of their rights related to assessment statute extension requests.
  - A. Reviewed the Examination Internal Revenue Manual (IRM), IRS memoranda and regulations, and the Appeals IRM and other Appeals guidelines to determine the policies and procedures for processing requests to extend the assessment statute of limitations.
  - B. Reviewed a sample of Business Master File (BMF)<sup>1</sup> and Individual Master File (IMF)<sup>2</sup> tax returns with taxpayer consents to extend assessment statutes processed from September 30, 2001, to October 5, 2002.
    1. Obtained BMF and IMF extracts to identify a population of tax returns having extensions of the assessment statute of limitations. The identified tax return populations were 15,242 and 36,403, respectively. We selected those extensions processed during cycles 200140 through 200240, which included September 30, 2001, to October 5, 2002. The IRS processes data in 1-week cycles.
    2. Analyzed the BMF and IMF records to identify assessment statute adjustments that could have resulted from extensions by the written consents of taxpayers (assessment statutes are often extended for reasons other than the taxpayer's written consent). For example, all tax returns for which a *Statutory Notice of Deficiency*<sup>3</sup> (Letter 3219) has been issued have the assessment statute extended for 150 days by law.
    3. Selected a statistical sample of 618 tax returns for review from the category of cases likely to have statute extensions by taxpayer consents from the Examination

---

<sup>1</sup> The BMF is the IRS database that consists of Federal tax-related transactions and business accounts. These include employment taxes, income taxes on businesses, and excise taxes.

<sup>2</sup> The IMF is the IRS database that maintains transactions or records of individual tax accounts.

<sup>3</sup> This is the final notice the IRS issues to taxpayers before it assesses additional tax when taxpayers either do not agree or do not respond to a request for information during an examination of a tax return.

## **Fiscal Year 2003 Statutory Audit of Compliance With Notifying Taxpayers of Their Rights When Requested to Extend the Assessment Statute**

---

and Appeals processes. However, we did not receive all requested tax returns and related cases, and time constraints prohibited us from reviewing all selected cases. We reviewed 482 tax returns and related cases, eliminating 329 tax returns from our sample that did not meet our criteria. Therefore, only 153 tax returns and related cases reviewed met the audit criteria. This was not sufficient for a statistical sample. Within this judgmental sample of 153 tax returns, there were 59 jointly filed returns and 109 returns for which the taxpayers had made a declaration of representation.<sup>4</sup>

4. Identified which business unit or function requested the extension and discussed any questionable extensions identified with IRS management for concurrence or an explanation of why the IRS felt that proper procedures were followed.
  5. Validated the IMF and BMF data for the following 5 fields on a randomly selected sample of 50 tax returns:
    - a) Transaction Code (TC)<sup>5</sup> 150<sup>6</sup> Received Date.
    - b) TC 560<sup>7</sup> Transaction Date.
    - c) Assessment Statute Expiration Date.
    - d) Tax Period.
    - e) Taxpayer Identification Number.
- II. Reviewed the selected tax returns and case files for documentation verifying that both taxpayers on jointly filed returns were separately advised of their rights related to statute extensions.
- III. Determined whether the Examination Quality Measurement System identified instances of noncompliance with the notice requirements when obtaining consent to extend the assessment statute. This sub-objective was included to help determine a possible cause should we have exceptions.
- IV. Determined the status of the IRS corrective actions proposed to address the recommendations presented in the prior Treasury Inspector General for Tax Administration audit reports.

---

<sup>4</sup> Some of the 153 sampled tax returns and related case files met multiple criteria.

<sup>5</sup> A transaction code is a three-digit code used to identify actions being taken on a taxpayer's account.

<sup>6</sup> The TC 150 posts to a taxpayer's account when a return is filed and a tax liability is assessed.

<sup>7</sup> The TC 560 posts to a taxpayer's account when the Assessment Statute Expiration Date is extended.

**Major Contributors to This Report**

Michael R. Phillips, Assistant Inspector General for Audit (Wage and Investment Income Programs)

Augusta R. Cook, Director

Paula W. Johnson, Audit Manager

Linda Bryant, Senior Auditor

Lynn Faulkner, Senior Auditor

John Hawkins, Senior Auditor

Sharon Shepherd, Senior Auditor

Jean Bell, Auditor

Vacenessia Daniels Brown, Auditor

Patricia Jackson, Auditor

Sylvia Sloan-Copeland, Auditor

Arlene Feskanich, Information Technology Specialist

**Fiscal Year 2003 Statutory Audit of Compliance With Notifying Taxpayers  
of Their Rights When Requested to Extend the Assessment Statute**

---

**Appendix III**

**Report Distribution List**

Deputy Commissioner for Operations Support N:OS  
Deputy Commissioner for Services and Enforcement N:SE  
Commissioner, Large and Mid-Size Business Division LM  
Commissioner, Small Business/Self-Employed Division S  
Commissioner, Tax Exempt and Government Entities Division T  
Commissioner, Wage and Investment Division W  
Chief, Appeals AP  
Deputy Commissioner, Large and Mid-Size Business Division LM  
Deputy Commissioner, Tax Exempt and Government Entities Division T  
Deputy Commissioner, Wage and Investment Division W  
Acting Deputy Commissioner, Small Business/Self-Employed Division S  
Director, Communications & Liaison, Small Business/Self-Employed Division S:M:C&L  
Director, Compliance, Small Business/Self-Employed Division S:C  
Director, Exempt Organizations, Tax Exempt and Government Entities Division T:EO  
Director, Field Assistance, Wage and Investment Division W:CAR:FA  
Director, Field Specialists, Large and Mid-Size Business Division LM:FS  
Director, General Appeals Program AP:G  
Director, Reporting Compliance, Small Business/Self-Employed Division S:C:CS  
Director, Strategy and Finance, Wage and Investment Division W:S  
Chief Counsel CC  
National Taxpayer Advocate TA  
Director, Office of Legislative Affairs CL:LA  
Director, Office of Program Evaluation and Risk Analysis N:ADC:R:O  
Office of Management Controls N:CFO:AR:M  
Audit Liaisons:  
    Commissioner, Large and Mid-Size Business Division LM:CL  
    Commissioner, Tax Exempt and Government Entities Division T:CL  
    Chief, Appeals AP:P:S  
    Chief, Customer Liaison, Small Business/Self-Employed Division S:COM  
    GAO/TIGTA Liaison W:S:PA



## **Fiscal Year 2003 Statutory Audit of Compliance With Notifying Taxpayers of Their Rights When Requested to Extend the Assessment Statute**

---

### **Appendix IV**

#### **Outcome Measures**

This appendix presents detailed information on the measurable impact on tax administration that the recommendation from the Treasury Inspector General for Tax Administration's Fiscal Year 2001 audit report<sup>1</sup> will continue to provide. These benefits will be incorporated into our Semiannual Report to the Congress.

##### Type and Value of Outcome Measure:

- Taxpayer Rights and Entitlements – Potential; Internal Revenue Code Section (§) 6501(c)(4)(B) (Supp. IV 1998); 40 of 153 taxpayer accounts affected (see page 3).
- Taxpayer Rights and Entitlements – Potential; Internal Revenue Service (IRS) Restructuring and Reform Act of 1998<sup>2</sup> § 3201; 37 of 59 jointly filed accounts affected (see page 6).
- Taxpayer Rights and Entitlements – Potential; 26 Code of Federal Regulations (C.F.R.) § 601.506;<sup>3</sup> 57 of 109 tax accounts where the taxpayers declared a representative (see page 7).

##### Methodology Used to Measure the Reported Benefit:

We reviewed a judgmental sample of 153 tax returns with consents to extend the assessment statute of limitations period. The returns were identified from the Fiscal Year 2002 Individual Master File (IMF)<sup>4</sup> and Business Master File (BMF)<sup>5</sup> databases. The review showed taxpayer rights were potentially affected in 64 of 153 tax returns sampled (42 percent). Each sampled tax return and related case file could have multiple findings for each criterion. Related case files were not documented in 40 of the 153 taxpayer accounts to show that the taxpayers or their representatives received their rights to refuse or to restrict the scope of the statute extensions. There was no documentation in the related case files that each taxpayer listed on the return was separately informed of his or her rights in 37 of 59 jointly filed accounts. In addition, in 57 of 109 tax accounts where taxpayers made declarations of representation, there was no documentation in the related case files that the IRS had provided both the taxpayers and the representatives with the advice of rights.

---

<sup>1</sup> *Most Taxpayers Are Advised of Their Rights Before Signing an Agreement to Extend the Assessment Statute of Limitations* (Reference Number 2001-10-157, dated September 2001).

<sup>2</sup> Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

<sup>3</sup> 26 C.F.R. § 601.506 (2001).

<sup>4</sup> The IMF is the IRS database that maintains transactions or records of individual tax accounts.

<sup>5</sup> The BMF is the IRS database that consists of Federal tax-related transactions and business accounts. These include employment taxes, income taxes on businesses, and excise taxes.

**Fiscal Year 2003 Statutory Audit of Compliance With Notifying Taxpayers  
of Their Rights When Requested to Extend the Assessment Statute**

---

**Appendix V**

**Case Review Results by Division**

	<b>Appeals</b>	<b>LMSB<sup>1</sup></b>	<b>SB/SE<sup>2</sup></b>	<b>TE/GE<sup>3</sup></b>	<b>Total<sup>4</sup></b>
<b>Number of Cases Reviewed</b>	18	30	101	4	153
<b>Compliance With Requirement to Notify Taxpayers of Their Rights</b>					
Number of Cases Where There Was No Evidence the Taxpayer Was Advised of Rights	1	7	14	1	23
Number of Cases Where the Taxpayer Was Previously Notified but Not Notified for the Extension in Our Sample	3	7	7	0	17
<b>Compliance With Internal Guidelines or Regulations</b>					
Number of Cases Not Meeting Documentation Requirements (Applicable Cases: 153) <sup>5</sup>	13	25	74	2	114
Number of Cases Where There Was No Documentation That Separate Notices Were Sent to Both Joint Filers (Applicable Cases: 59)	8	6	22	1	37
Number of Cases Where There Was No Evidence That Notices Were Given to Both the Taxpayer and Representative (Applicable Cases: 109)	11	15	30	1	57

---

<sup>1</sup> Large and Mid-Size Business Division.

<sup>2</sup> Small Business/Self-Employed Division.

<sup>3</sup> Tax Exempt and Government Entities Division.

<sup>4</sup> No cases from the Wage and Investment Division occurred in our sample.

<sup>5</sup> All cases do not have the same requirements. For example, all cases have a documentation requirement; however, not all cases involve taxpayer representatives or those who file joint returns.

**Listing of Prior Reports on Compliance With Notifying Taxpayers  
of Their Rights When Requested to Extend the Assessment Statute**

*Information Provided to Taxpayers When Requesting Extensions of the Assessment Statute of Limitations Can Be Improved* (Reference Number 2000-10-142, dated September 2000).

*Most Taxpayers Are Advised of Their Rights Before Signing an Agreement to Extend the Assessment Statute of Limitations* (Reference Number 2001-10-157, dated September 2001).

*Improved Documentation Is Needed to Ensure Taxpayers Are Informed of Their Rights When Requested to Extend the Assessment Statute* (Reference Number 2002-40-175, dated September 2002).

**Fiscal Year 2003 Statutory Audit of Compliance With Notifying Taxpayers  
of Their Rights When Requested to Extend the Assessment Statute**

---

**Appendix VII**

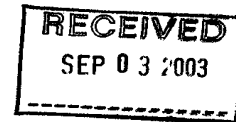
**Management's Response to the Draft Report**



COMMISSIONER  
SMALL BUSINESS/SELF-EMPLOYED DIVISION

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

AUG 27 2003



**MEMORANDUM FOR TREASURY INSPECTOR GENERAL FOR TAX  
ADMINISTRATION**

**FROM:** Dale F. Hart *Dale Hart by MSW*  
Commissioner, Small Business/Self-Employed Division

**SUBJECT:** Draft Audit Report – Fiscal Year 2003 Statutory Audit of  
Compliance With Notifying Taxpayers of Their Rights  
When Requested to Extend the Assessment Statute  
(Audit # 200240065)

The Congress enacted Internal Revenue Code (IRC) Section 6501(c)(4)(B) to ensure the Service adequately advises taxpayers of their rights when we request consents to extend the assessment statute. IRC 6501(c)(4)(B) also requires the annual review by TIGTA of our compliance with this section.

As in prior years, this year's review acknowledges that, in most situations, we are appropriately advising taxpayers and representatives of their rights. Some of the returns you reviewed lacked specific written documentation indicating that we had advised taxpayers of their rights. As part of our follow-up review we found other documentation in the case file that showed that the taxpayer had received satisfactory notification of their rights.

We continue to reinforce the requirement to document our actions in the case files. On February 28, 2003, we issued additional guidance to supplement and reinforce this requirement to our employees. We will continue to monitor this area as part of our regular review process.

If you have any questions or need additional information, please contact me at (202) 622-0600 or Joseph R. Brimacombe, Deputy Director, Compliance Policy, at (202) 283-2200.